



Utilities

2Q20 Earnings Preview (Correction*)

Summary:

We expect strong 2Q20 earnings prints for electric utilities thanks to strong residential electric sales, sooner-than expected recovery in C&I loads, and aggressive cost-cutting. Consensus estimates look stale to us, but we expect the strongest positive surprises from MI utilities, **CMS** and **DTE**, though no increase in the 2020 EPS guidance for **DTE** at this point, **SRE**, thanks to tax benefits and cost efficiencies at SDG&E/SoCalGas, and **AEP**, thanks to aggressive cost-cutting which started before COVID. We struggle to call **ETR** results.

There should be plenty of volatility in earnings of water stocks, **CWT** and **AWR** in particular, and that's even before CA makes changes to the revenue decoupling mechanism (WRAM). There should be few surprises from **AWK** and **WTRG**. We chase **AWK** and raise our price target to \$145.50 from \$130.

Power/retail stocks in TX, **NRG** and **VST**, should report very strong results even though we have yet to see scarcity in spot power prices in ERCOT. Thanks to solid 1H20 results both **NRG** and **VST** should be tracking ahead of the midpoint of their 2020 EBITDA guidance ranges, but we don't expect them to narrow/raise the guidance just yet. We raised our 2021/2022 EBITDA estimates for **VST** to reflect additional hedges.

We updated 2Q20 earnings estimates for: **AEP, AES, AGR, ATO, AWK, AWR, CMS, CWT, D, DTE, DUK, EIX, ES, ETR, EXC, FE, NRG, PCG, PEG, PPL, SJW, SO, SRE, VST** and **WTRG**. We also increased our price target for **AWK**.

(*Correction made to the original version of this note: Our 2Q20 estimate for PEG displayed on page 3 has been corrected.)

Highlights

Electric/gas utilities

An earlier than expected recovery in C&I loads coupled with cost-cutting and some YoY weather benefit should deliver strong earnings beats for MI utilities, **CMS** and **DTE**, in our view. **AEP's** aggressive cost-cutting started pre-COVID should support 2Q20 results while the load weakness should be largely in-line with management's forecasts from the 1Q20 call. The company plans to provide an updated capex and cash flow schedule through 2023 which should incorporate lower capex in 2020 and the \$2B North Central Wind project (and its financing). **D** and **SO** should have some weather-related headwinds in 2Q20, but updates on the Vogtle cost schedule (Unit 3 % completion in May and June) and cost contingency being utilized should dominate **SO's** earnings call. **SO** kept its May 2021 in-service date for Vogtle unit 3 to help with managing the scheduling of the construction work on the site, but the decision has not been well-received by investors. **DUK** plans to provide an update on its capex replacement for the cancelled ACP pipeline only on the 4Q20 earnings call, but we'd expect the replacement for the \$2B capex reduction to start only in 2022.

Water utilities

AWK and **WTRG** should have relatively easy YoY comps in the Northeast/Mid-Atlantic as 2Q19 was very rainy, and **WTRG** now has additional cost levers thanks to the Peoples Gas merger. We don't expect any meaningful COVID impacts on their 2Q20 or annual 2020 earnings. Intervener testimonies in **AWK's** NJ rate case should be made public any day now – this rate case together with similar proceedings in PA and MO should dominate **AWK's** earnings call. We are chasing **AWK's** stock by raising our price target to \$145.50 from \$130 previously.

WTRG's pending acquisition of the Delcora wastewater system in PA has run into legal issues, making investors concerned about the future of municipal water/wastewater M&A.

In CA, Commissioner Guzman Aceves has yet again proposed to do away with the current full revenue decoupling mechanism (WRAM) for investor-owned water utilities, calling it ineffective at promoting water conservation. The CPUC should consider/vote on the proposed decision as soon as August 6. **AWR's** GSWC will have filed its new General Rate Case (GRC) by then while **CWT's** and **AWK's** GRCs in CA are already pending. We therefore assume that any changes to the WRAM, if any, would apply to these companies only in the next GRC, starting in 2024.

CWT keeps waiting for an approval of its GRC to record a revenue increase. In the meantime, **CWT's** quarterly results should continue to come well below expectations. We expect **AWR** to fully recoup the \$0.08 EPS hit recorded in 1Q20 related to the underperformance of its pension funds.

Power/retail

The TX load has recovered to pre-COVID levels and while we have seen no real scarcity in power prices so far this summer, strong retail results supported by lower than expected bad debt and optimization of generation hedges should support 2020 EBITDA for **VST** and **NRG** at least at the midpoint of their annual guidance. We don't expect them to narrow the guidance yet, however, as August tends to be a crucial earnings month for both companies.

NRG should provide an update on its 2020 capital allocation strategy which might include another retail acquisition. **VST** hasn't given up on some uplift to forward power curves in TX happening in late August/early September, like we saw last year. Yet, even without the recovery and thanks to additional power hedges, the downside to 2021 EBITDA seems now lower than the \$200-250MM below the midpoint of the 2020 guidance range that VST used to quote as a COVID-related downside scenario. Therefore, we raised our 2021/2022 EBITDA expectations for VST to \$3,135MM/3,044MM up from \$3,034MM/3,009MM, respectively.

We expect **AES** to keep its new/lowered EPS guidance range for 2020 though 2Q20 should be weak on a combination of the DPL/Argentina/IPL hits, with the earnings uplift from cost-cutting and Southland's PPA should kick in only in 3Q20. The OH and IN load seem to be performing ahead of management's expectations from the 1Q20 earnings call. We await an update on another divestiture of coal-fired plant, potentially Maritza in Bulgaria, we believe.

2Q20 EPS/EBITDA Estimates for Utilities and Power Stocks

Regulated electric/gas utilities	Seaport 2Q20 EPS (\$)	Consensus 2Q20 EPS (\$)	Seaport/Consensus
AEP	1.09	0.99	10%
AGR	0.36	0.33	9%
ATO	0.80	0.76	5%
CMS	0.46	0.36	28%
D	0.81	N/A	N/A
DTE	1.35	1.14	18%
DUK	1.05	1.02	3%
EIX	1.20	1.16	3%
ES	0.76	0.79	-4%
ETR	1.10	1.25	-12%
EXC	0.42	0.45	-7%
FE	0.56	0.55	2%
PCG	1.00	0.94	6%
PEG	0.57	0.62	-8%
PPL	0.55	0.56	-2%
SO	0.66	0.69	-4%
SRE	1.82	1.19	53%

Regulated water utilities	Seaport 2Q20 EPS (\$)	Consensus 2Q20 EPS (\$)	Seaport/Consensus
AWK	0.98	0.95	3%
AWR	0.70	0.63	11%
CWT	0.25	0.64	-61%
SJW	0.70	0.66	6%
WTRG	0.23	0.24	-4%

Power/retail	Seaport 2Q20 EPS/EBITDA \$/ \$MM	Consensus 2Q20 EPS/EBITDA \$/ \$MM	Seaport/Consensus
AES	0.22	0.28	-21%
NRG	550	521	6%
VST	840	729	15%

Source: FactSet for consensus, Seaport Global Securities

Comp Sheet: Utilities & Power

	Share price (\$)		Price target		Premium/Discount
Regulated electric utilities	7/15/2020	Rating	(\$)	2022 PE	to Avg 2022 P/E ex
AEP	84.68	Buy	91.00	16.8x	-5%
AGR	45.20	Neutral	N/A	17.3x	-2%
CMS	59.74	Buy	65.00	19.6x	11%
D	75.45	Buy	91.00	18.2x	3%
DTE	109.20	Buy	133.50	14.7x	-17%
DUK	80.43	Neutral	N/A	15.8x	-11%
EIX	55.28	Buy	70.00	10.2x	-42%
ES	85.00	Buy	93.00	20.6x	17%
ETR	96.24	Buy	114.00	15.2x	-14%
EXC	38.05	Buy	44.00	14.0x	-21%
FE	40.82	Buy	50.00	14.8x	-16%
PCG	9.20	Neutral	50.00	8.5x	-52%
PEG	52.40	Neutral	N/A	15.4x	-13%
PPL	25.69	Sell	25.00	14.3x	-19%
SO	53.02	Buy	63.00	14.9x	-16%
SRE	123.15	Buy	142.00	15.0x	-15%
Average P/E for regulated electrics with exclusions				17.7x	
	Share price (\$)		Price target		Premium/Discount
Regulated water utilities	7/15/2020	Rating	(\$)	2022 PE	to Avg 2022 P/E ex
AWK	134.06	Buy	145.50	29.2x	9%
AWR	77.21	Buy	84.00	29.9x	12%
CWT	48.00	Neutral	N/A	26.4x	-1%
SJW	62.63	Neutral	N/A	23.7x	-11%
WTRG	43.04	Neutral	N/A	24.4x	-9%
Average P/E for regulated water utilities				26.7x	51%
	Share price (\$)		Price target		Premium/Discount
Power/retail	7/15/2020	Rating	(\$)	2022 PE/FCF yield	to Avg 2022 P/E ex
AES	15.07	Buy	17.00	9.1x	N/A
NRG	34.02	Buy	42.50	16.7%	N/A
VST	19.30	Buy	24.00	20.0%	N/A

Source: FactSet, Seaport Global Securities

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Other Companies Mentioned in This Report

- CMS Energy Corporation (CMS: \$59.74, Buy)
- Sempra Energy (SRE: \$123.15, Buy)
- NRG Energy, Inc. (NRG: \$34.02, Buy)
- Entergy Corporation (ETR: \$96.24, Buy)
- Vistra Energy Corp. (VST: \$19.30, Buy)
- American States Water Company (AWR: \$77.21, Buy)
- Essential Utilities, Inc. (WTRG: \$43.04, Neutral)
- Duke Energy Corp. (DUK: \$80.43, Neutral)
- Atmos Energy Corp. (ATO: \$100.64, Buy)
- Eversource Energy (ES: \$85.00, Buy)
- FirstEnergy Corp. (FE: \$40.82, Buy)
- Public Service Enterprise Group Inc. (PEG: \$52.40, Neutral)
- SJW Group (SJW: \$62.63, Neutral)
- DTE Energy Company (DTE: \$109.20, Buy)
- Southern Co. (SO: \$53.02, Buy)
- American Electric Power Company, Inc. (AEP: \$84.68, Buy)
- California Water Services Group (CWT: \$48.00, Neutral)
- American Water Works Company, Inc. (AWK: \$134.06, Buy)
- AES Corporation (AES: \$15.07, Buy)
- Dominion Energy, Inc. (D: \$75.45, Buy)
- Avangrid, Inc. (AGR: \$45.20, Neutral)
- Edison International (EIX: \$55.28, Buy)
- Exelon Corporation (EXC: \$38.05, Buy)
- PG&E Corporation (PCG: \$9.20, Neutral)
- PPL Corporation (PPL: \$25.69, Sell)

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Neutral	42	34.1%	0	0.0%	0.0%
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Total	123	100.0%	3	100.0%	2.4%

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